

**Prepared Statement of  
George A. Ray  
Chairman & CEO  
LeFiell Manufacturing Company  
To  
Subcommittee on Financial Institutions  
And Consumer Credit of  
House of Representative  
Committee on Financial Services**

**Hearing on Financing of Employee Ownership:  
An Overview**

**June 10, 2003  
2:00 PM  
2128 Rayburn House Office Building  
Washington, DC**

Statement George A. Ray, Chair and CEO, LeFiell Manufacturing  
At Hearing of Subcommittee on Financial Institutions and  
Consumer Credit of the Committee on Financial Services  
On Financing Employee Ownership: An Overview

Chair Bachus, Ranking member Congressman Sanders, and members of the Subcommittee on Financial Institutions and Consumer Credit.

First I thank Congressman Royce for his kind introduction. Back in California we all know and appreciate the work Ed Royce does for the betterment of our communities and their people.

As Chair of The ESOP Association, the national trade association representing companies with ESOPs, the ESOP community is very excited that the subcommittee is holding this hearing. We know, and appreciate that Congressman Sanders has worked with several outstanding companies in Vermont, who are prime examples of the power of employee ownership, has pushed open the door to review how this nation can finance more employee ownership. I am proud to sit here today with a representative of one of those companies, Sherri Ceresa, Gardeners Supply, Burlington, Vermont. To demonstrate how much The ESOP Association values our outstanding Vermont employee-owned companies, our small ten-person board has two Vermont ESOP company leaders as members.

I started with LeFiell Manufacturing in 1962 at \$1.75 an hour working as a machine operator. Today I am Chairman and CEO, a post I have held since 1992.

I will give a brief background on LeFiell, the story of our employee ownership journey, and what we have experienced in terms of financing our transition of being conventionally owned to being employee-owned through an ESOP, and conclude with a brief comment about employee ownership in the 21<sup>st</sup> Century.

LeFiell Manufacturing traces its beginnings to 1930, when Mr. LeFiell began a gray iron foundry and small machine shop business on Vernon Avenue in Los Angeles. From 1930 to 1954 its primary business was supporting the meat packing industry and its customers were the large meat packing companies.

In the 1950's the company began to transform itself, and began to produce structural parts for the aircraft industry. When I joined the company in 1962, its primary work was in that industry, and its primary customers were the large aircraft companies like the Donald Douglas, Convair, and Boeing. At that time, we had about 40 people. Today, LeFiell is 110 employee owners strong and is the leading supplier of precision tubular parts and assemblies for the aerospace industry. A few examples- - we produce six miles of liquid hydrogen fuel lines for each Space Shuttle; we have assisted in the design and have manufactured the tubular structure for sixty feet of the Space Station, and today, to the best of our knowledge, LeFiell supplies all fuel lines for every liquid hydrogen engine used on expendable rockets to launch satellites in the United States and Japan.

Mr. LeFiell was a difficult person to work for on a day-to-day basis, as he was very demanding on attention to details for whatever you were working on, but he was generous when it came to sharing the company.

In 1954 he incorporated to a privately held California C Corporation so he could give some shares of the company to key employees and also allow employees who wanted to invest in the company to purchase through a payroll deduction plan. In 1974, when the legislation to allow the creation of ESOP's was enacted by Congress, LeFiell was one of the first companies in the United States to form an ESOP. It was a perfect fit to carry on the LeFiell sharing culture. Mr. LeFiell had retired by this time and new employees were leading the company.

From 1974 thru 1986 the ESOP growth was funded with company earnings and company credit line funds. By 1986 the ESOP had accumulated 30% ownership in the company, with current and retired employees owned the balance. In 1987, a new strategy was initiated to purchase stock from retired employees, and today the ESOP has 67% ownership. There are over 250 owners of LeFiell and it would take the forty top shareholders with private and ESOP shares to make-up 50% of the stock today. That's broad-based ownership! Today we are studying a plan to purchase the balance of the shares in the next 12 months and become 100% owned by the employee ESOP. This will require the ESOP to borrow with the company guarantee of the loan and a plan to pay the loan off over a number of years. It has been a wonderful journey for me, my family and all of the employee owners of LeFiell where each employee has received a major benefit for retirement from the company they helped build.

"Has an ESOP been good for our employees, and LeFiell"? Yes sir, and let me give you some examples. The average employee owner at LeFiell has an account balance of \$129,000, nineteen employees with twenty-one to twenty-five years of service have average account balances of \$217,000 and eleven employees who have over twenty-five years of service have account balances of \$357,000. This will certainly contribute to a much happier retirement for these employees and their families when they are ready to retire.

As the President of The ESOP Association said earlier, ever since the beginnings of ESOPs in the late 50's, and certainly with enactment of laws in the 1980's encouraging exiting owners from private businesses to sell to ESOPs, 75 to 80% of the ESOPs created in America are the result of existing owners selling their stock to an ESOP.

Casual observers of the American economy, perhaps fixated on reading the *Wall Street Journal*, or watching the TV cable news with reports on how the stock market did, do not appreciate that over 50% of Americans work for companies that do not have publicly traded stock, and that 95% of the businesses in America are not publicly traded. And even those who understand this fact of the dominance of private companies, really do not appreciate that sooner or later, the owners of these private companies, have to cash out of the company.

When LeFiell in 1974 established its ESOP, like 80 to 85% of the companies then, we did not formally include the ESOP in the financing transaction. We used the corporation's credit, borrowed money, bought stock from Mr. LeFiell, and made contributions to a stock bonus plan from the purchased block of stock, which we held in Treasury. We also printed new shares of

LeFiell treasury stock to contribute to the ESOP. As Michael Keeling explained, tax laws enacted in 1984 and 1986 triggered companies to leverage their ESOPs formally, where debt was supported by the ESOP, and the stock all goes into an ESOP suspense account. This is the method LeFiell is currently considering to purchase the last 33% for the ESOP. There are advantages and disadvantages to either style, but again, since the mid-80's, most ESOPs are "leveraged", and employees get the financial advantage of stock appreciation as the leverage is paid down.

Whether done on corporate credit, or with a leveraged ESOP, the ESOP creates an excellent option for the transaction involving the current owners of private business cashing out of their stock, or ownership position.

Being an Employee Owned-ESOP Company has had many business benefits for us over the years. Our customers recognize the value of a stable company that has been in business for seventy-two years; the auditors from the government who review our government contracts have never questioned our contributions to our ESOP. I believe they recognize the value and legitimate expense of a broad-based employee retirement program through an ESOP.

Chairman Bachus, and members, I know that your full committee oversees the nation's accounting standards, and has reviewed work and proposals of the Financial Accounting Standards Board, or FASB. Oddly enough, the manner in which the accounting standards treat ESOPs in instances of healthy companies might impact employee-owned companies getting financing more than whether money is available. These accounting standards go back to 1976, with the most recent standards being issued in 1993. There is no question in my mind that the 1993 accounting standards hinder the creation of ESOPs.

But even more troubling, we now have FASB issuing standards that are not precisely directed at ESOPs, and their impact may be so drastic that the standard makes the ESOP company look financially unhealthy, when in fact the cash flow statement proves otherwise. The standard, recently release FASB 150, was issued without any input from the ESOP community.

I am not an accountant, and today's hearings are not about the accounting treatment of ESOPs.

I wish to make two comments, however: One, our problems are not about reporting the ESOP stock compensation as an expense, which is the debate in the stock option arena that your committee had hearings on. ESOPs contributions are reported as an expense. New standard FASB 150, some say, will wipe out the value of employee-owned companies through ESOPs, in some instances by 100%. An ESOP cannot get financing when it shows all of its equity as a liability. Two, Mr. Chairman and members, I would ask that as the ESOP community comes to understand FASB 150 better, you keep an open door to hear us out, and to see if we need to put more focus on accounting standards that, contrary to the intent of Congress, may snuff out employee ownership through ESOPs.

In conclusion, let me summarize my statement: One, the experience of LeFiell Manufacturing with employee ownership through ESOPs is very positive. As Chair of The ESOP Association, and former President of the California chapter of ESOP companies, I can say my personal

experience with other ESOP companies convinces me that LeFiell's experience is not unique. I would state that LeFiell has not had significant issues in getting financing for its ESOP creation and expansion, nor have we had problems with ongoing financing because we are an ESOP. Let me quickly add, LeFiell's experience, and those of other companies that are ESOPs that I know of, are nearly all strong financially and good candidates to pay lenders back their loans with the interest.

I do have a concern that a recent accounting standard will make it harder to explain the true financial situation of an ESOP company. And it may make it difficult for companies to obtain financing from lenders to execute a leveraged buy-out or raise capital for company expansion.

Finally, we do believe that there are many areas of our nation's ownership, and employee ownership policies that need consolidation. We believe our ownership policies need more support and focus by the Executive Branch.

We believe that your hearing is sending a signal that employee ownership is more important to the well-being of our economy and our employees than arcane tax laws, or hard to fathom retirement income security laws, or the ERISA laws. Your hearing reveals areas that need more review. I believe, however, if the Financial Services Committee commits to ownership we will see more financing available to those companies, that might not make it otherwise, enabling them to become employee owned, like LeFiell Manufacturing.